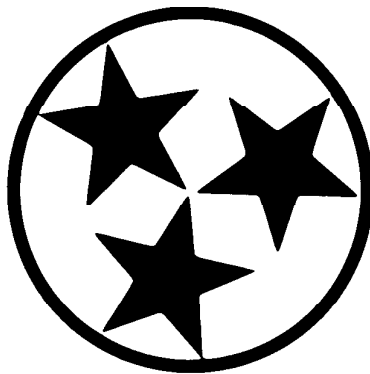


Tennessee Subrecipient Monitoring Manual



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§ Introduction §

The federal Office of Management and Budget (OMB) issued Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, June 1997. This circular supersedes Circular A-133, *Audits of Institutions of Higher Education and Other Non-Profit Institutions*, and Circular A-128, *Audits of State and Local Governments*. The revision raises the audit threshold of subrecipients expending federal funds from \$25,000 to \$300,000 increasing the number of subrecipients exempt from audit when federal expenditures are less than \$300,000. The revision also prohibits charges to federal awards for the costs of a single audit for subrecipients expending less than \$300,000. However, the revision allows states to charge subrecipient monitoring costs or the costs of agreed-upon procedures to federal awards provided that the monitoring procedures and/or audits are of lesser scope than a single audit.

OMB Circular A-133, Section -400(d), discusses the various responsibilities of the pass-through entity, i.e., the state. The responsibility for monitoring is explained in subparagraph (3) of this section which states that the pass-through entity is required to “monitor the activities of subrecipients as necessary to ensure that federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.” In order to comply with the provisions of OMB Circular A-133, the state

has made appropriate changes in agreements with subrecipients to reflect that single and program-specific audits are no longer required for subrecipients expending less than \$300,000 annually;

has reviewed the overall monitoring process, and is requiring uniform statewide monitoring procedures to ensure subrecipient compliance;

has taken into consideration the cost-effectiveness of monitoring procedures compared to the relative size and complexity of the federal awards administered by subrecipients in determining the appropriateness of monitoring procedures.

OMB Circular A-133 and the Single Audit Act Amendments of 1996 require states to monitor subrecipients to ensure that federal funds are used appropriately. The State of Tennessee has chosen to treat state and federal dollars alike in the area of monitoring. Any entity meeting the subrecipient criteria will be subject to monitoring including private non-profit entities, for-profit entities, governmental entities, and state and local governments. In response to the revision of OMB Circular A-133 and the results of a Department of Finance and Administration 1996 survey of state monitoring activities, the state has developed an approach to monitoring which ensures uniform monitoring of subrecipients. The foundation of this approach is based on OMB Circular A-133 Compliance Supplement. Uniformity is brought to monitoring through the development of core areas.

The coordinated monitoring approach is aimed at targeting resources to areas of greater risk, obtaining better information, and reducing audit costs. The revised OMB Circular A-133 and the survey results have compelled the state to examine monitoring activities of all state departments, agencies, and commissions (hereafter referred to as state agency) and to ensure that all subrecipients are adequately monitored. The Department of Finance and Administration in a collaborative effort with the Comptroller of the Treasury's Office has identified the need for a coordinated system to address statewide monitoring issues.

§ Purpose and Applicability §

The purpose of this document is to serve as a guide in monitoring state and/or federal funded programs administered by subrecipients. It is intended to identify important requirements that the state, as both a grantor and pass-through entity for program funds, should monitor and provide reasonable assurance that subrecipients are in compliance with all applicable requirements.

This manual is structured to provide consistency in the monitoring activities across various state agencies and to ensure that core monitoring areas are performed by monitoring groups. The manual provides assistance in the development of a monitoring plan. It also identifies minimum monitoring requirements along with a set of core areas common to most state and/or federal awards. The core areas are consistent with requirements of OMB Circular A-110, *Uniform Administrative Requirements for Grants and Other Agreements With Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations*; OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Government*; OMB Circular A-122, *Cost Principles For Non-Profit Organization*; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

§ Coordinated Monitoring Approach §

The primary objective of a coordinated approach to monitoring within the state is to increase the level of and to encourage uniform monitoring of subrecipients regardless of the state and/or federal program. Policy 22 will assist in meeting this objective by requiring each state agency to have a well-documented monitoring plan that ensures compliance with applicable state and/or federal monitoring requirements.

The revision of OMB Circular A-133 and the results of a 1996 Finance and Administration survey of monitoring activities present good reasons for a coordinated monitoring system. This coordinated systematic approach will consist of the following:

A statewide monitoring policy, manual, and plan.

The coordination of efforts among the Department of Finance and Administration, Division of Resource Development and Support; Comptroller of the Treasury, Divisions of State Audit, Municipal Audit, and County Audit; and state agencies. This coordination is necessary to ensure adequate coverage without duplication and reduces the burden on subrecipients.

A centralized monitoring team in the Division of Resource Development and Support to provide monitoring services and technical assistance to state agencies.

The development of a subrecipient database. This database will make available pertinent information about each subrecipient including but not limited to the name, address, sources of funds, monitoring findings, audit findings, corrective action status, licensure status, status of charter, expenditures.

The Division of Resource Development and Support (RDS) is the coordinating point for the statewide monitoring system. This division is within the Department of Finance and Administration. RDS houses the offices of Contract Review, Criminal Justice Programs, Financial Systems Consulting Group, National and Community Service Commission, and Program Evaluation. The Division provides services to promote the quality management of state and federal resources in partnership with public and private agencies. As the coordinating point, the division will

design, implement, and manage a statewide coordinated monitoring system,
determine monitoring activities and staff to be consolidated and centralized,
provide monitoring services to other state agencies,
review, comment on and approve monitoring plans submitted by state agencies,
provide training and technical assistance on fiscal and program monitoring issues,
develop and maintain a subrecipient management information database.

§ Required Monitoring Plan §

Department of Finance and Administration Policy 22 requires state agencies that fund subrecipients to develop a plan to address their monitoring needs. The plan should identify all subrecipients under contract, describe the process and risk criteria used to select and prioritize the subrecipients for monitoring purposes, include sample monitoring manuals for each state and/or federal program and identify a staffing plan. The monitoring plan may be for one, two, or three years unless otherwise specified by state and/or federal guidelines. For example, a three-year plan may include subrecipients that would be monitored every year because of their high risk level, while other subrecipients identified in the plan may be monitored once every two or three years depending on their respective risk levels. The frequency of monitoring will be determined by the state agency. In situations where more than one state agency monitors the same subrecipient, the frequency of the monitoring will be mutually agreed upon through discussions with the Department of Finance and Administration, Resource Development and Support Division.

For the purpose of this plan, “monitoring” is defined as the review process used to determine a subrecipient’s compliance with the requirements of a state and/or federal program, applicable laws and regulations, and stated results and outcomes. Monitoring identifies operational changes and determines that internal control over financial management and accounting systems are adequate to account for program funds in accordance with state and/or federal requirements.

Subrecipient Identification--The monitoring plan should identify all subrecipients in a contractual relationship with the state agency. A subrecipient is a non-federal entity that expends state and/or federal funds received from the state to carry out a state and/or federal program. A subrecipient is not a vendor because program compliance requirements usually do not pass through to vendors. Therefore, state agencies are not required to include vendors in their monitoring plan.

There may be unusual circumstances or exceptions to the characteristics of subrecipients and vendors. In making the determination of whether a subrecipient or vendor relationship exists, the substance of the relationship is more important than the form of the agreement. It is not expected that all subrecipient characteristics will be present. Judgment should be used in determining whether an entity is a subrecipient or a vendor. If the contractual relationship with the state meets the vendor criteria, then the state agency must ensure that the procurement, receipt, and payment for goods and services comply with laws, regulations, and the provisions of the contract.

To distinguish a subrecipient from a vendor, use the characteristics below from OMB Circular A-133, Section .210.

Subrecipient Characteristics	Vendor Characteristics
<p>Determines who is eligible to receive state and/or federal financial assistance available through the program administered</p> <p>Has its performance measured against whether the objectives of the state and /or federal program are met</p> <p>Has responsibility for programmatic decision making</p> <p>Has responsibility for adherence to applicable state and/or federal program compliance requirements</p> <p>Uses state and/or federal funds to carry out a program of the state as compared to providing goods or services for a program of the state</p>	<p>Provides the goods and services to many different purchasers</p> <p>Provides goods and services within normal business operations</p> <p>Operates in a competitive environment</p> <p>Provides goods or services that are ancillary to the operation of the state and/or federal program</p> <p>Is not subject to compliance requirements of the state and/or federal program</p>

Risk-based Selection--After determining the population required to be monitored, each state agency should define risk criteria that are applicable to its specific programs. One way to determine risk is to use an assessment tool. A risk assessment is useful in determining the priority of subrecipients to be reviewed and the level of monitoring to be performed. Also, the risk assessment can help determine how often each subrecipient should be monitored.

Attachment E is an example of a risk assessment that involves the evaluation of several factors, such as operating systems, internal controls, board of directors' involvement, contract experience with the state and/or federal government, and operational changes. When using a risk assessment, it should target areas that help identify the subrecipient's risk level, such as financial problems that could lead to diversion of program funds, loss of essential personnel, loss of license or accreditation to operate the program, rapid growth, new activities or services, organizational restructuring, and complaints regarding program and/or fiscal operations. Other information may be used in assessing the subrecipient's risk level such as historical information; anecdotal information from employees; clients, and participants; and anticipated changes. It is the responsibility of each state agency to define risk for each of its programs and how to assess it.

Monitoring Guides--A sample guide for each state and/or federal program that includes all monitoring requirements should be included in plan. The guide will serve as a summary of the monitor's work. Each state agency should develop monitoring guides that reflect the required monitoring core areas and that meet its program and fiscal needs.

Staffing Plan--Full-time equivalents and personnel classification should be identified for all staff monitoring subrecipients. There should be a separation of duties for all monitoring staff to ensure

independence and objectivity. For example, monitoring personnel should have duties that are segregated from program and fiscal management, program development, technical assistance, or any other function related directly to program administration. Before a state agency can contract with a third party for monitoring services, approval must be given by the Division of Resource Development and Support.

§ Required Monitoring Core Areas §

The type of monitoring is determined by the subrecipient's risk level. For each risk level, monitoring objectives and core areas have been identified. Each state agency must have monitoring procedures that meet the objectives of each risk level and core areas.

The **required** core monitoring areas are activities allowed or unallowed; civil rights; allowable cost/cost principles; eligibility, matching, level of effort, earmarking; program income; cash management; Davis-Bacon Act; equipment and real property management; period of availability of funds; procurement, suspension, and debarment; real property acquisition and relocation assistance; reporting; and special tests and provisions.

The monitoring of a subrecipient classified as high or medium risk should include testing of the financial/program data and reporting. For high risk subrecipients, the sample size should be larger than that of medium risk and the level of testing should be more intense. The following are the basic objectives of high-and medium risk monitoring:

- To obtain reasonable assurance that the agency is a going concern.

- To test the reliability of internal controls.

- To verify that program objectives are being met.

- To verify that civil rights requirements are being met.

- To test the reliability of the subrecipient's financial and programmatic reports.

- To test if costs and services are allowable and eligible.

The basic objective of low-risk monitoring is to assess internal and operational controls to determine if further monitoring is necessary.

§ Suggested Monitoring Techniques §

Meeting the monitoring objectives for high, medium, and low risk subrecipients can be achieved through a variety of monitoring techniques. The techniques listed below are suggested for testing the core monitoring areas for compliance. The suggested monitoring tests recommended are physical examination, confirmation, vouching, tracing, inquiry, observation, reperformance, reconciliation, inspection and analytical procedures.

Physical examination--Physical examination refers to gathering physical evidence and it provides the most reliable form of evidence. Therefore, observation of physical evidence may be required when testing high risk subrecipients such as counting petty cash, inspecting new equipment, observing inventory, determining staff/client ratio, or inspecting medications. However, reviewing invoices and/or other supporting documentation may satisfy the same objective when testing medium or low risk subrecipients.

Confirmation--Confirmation refers to the written requests to a particular third party to confirm assertions made by the subrecipient. It may include confirming the accounts receivable balance or confirming that an individual received service from a particular program, confirming civil rights compliance with appropriate federal/state agencies, or confirming policy waivers given by the state agency.

Vouching--Vouching is the examination of documents that support a recorded transaction, amount, or activity. Vouching helps to obtain evidence about a recorded transaction, and therefore cannot identify unrecorded transactions or activities. Vouching starts from the recorded transaction to the supporting evidence. Vouching may be used to verify the expenditure reports reported to the grantor or to the reliability of program results and achievements to supporting documentation.

Tracing --Tracing refers to verifying the recording of a document in the accounting records. Tracing is similar to vouching, except it starts with the document to the records. A monitor may use tracing to verify a transaction, such as an invoice, through the accounting system to its ultimate recording in the accounting records, journal, ledgers and to the appropriate grant program. A monitor may also use tracing to verify that incidents, runaways, or use of physical restraints was reported to the proper authorities and recorded in the client's record.

Inquiry--Inquiry is the test used to obtain management's and employees' responses to questions about the operations of the subrecipient. Monitors may use inquiries to get a better understanding of staffing patterns, levels of supervision, how services are delivered, management controls, and how a program is intended to operate. Inquiries usually provide the basis for further testing to substantiate the responses to the inquiries.

Observation--Observation is the witnessing of physical activities by the monitor such as taking of physical inventory, touring facilities, attending client staffings, or witnessing physical restraints. Monitors may also use this test to observe how a program is operated. Observation and inquiry should be used in testing monitoring areas when the monitor cannot review a document in any other manner. When the circumstance does not allow the monitor to review or test documentation, the monitor can make inquiry and observe the process to ensure that the intended controls are adequate or being implemented as intended. Inquiry of the process to gain an understanding of how it operates may be sufficient for a low risk subrecipient, however, the process may need to be observed in a high and/or medium risk subrecipient.

Reperformance--Reperformance is the process of testing the integrity of transactions or balances by

monitors to independently verify the reliability of the controls. Monitors may reperform some transactions and compare the results of the reperformance with expected results.

Reconciliation--Reconciliation is the process of matching two independent sets of records. Reconciliations serve to provide assurance of completeness and existence. Reconciliation may be necessary to confirm grant revenues and receivables in a high and/or medium risk subrecipient before closing out a program year.

Inspection--Inspection is the examination of documents other than vouching and tracing. Inspection is the critical reading of a document to compare the information therein with other information known to the monitor. This includes review of contracts, leases, insurance policies, program guidelines, minutes of board meetings and other pertinent records. Inspection may be used in all monitoring activities regardless of the risk level.

Analytical procedures--Analytical procedures encompass a number of specific tests that a monitor may use to test the reasonableness of data. A monitor may use analytical procedures, such as certain ratios and trends to determine any unusual conditions that indicate further testing is warranted. Analytical procedures may be used to provide some level of assurance of low risk subrecipients and may be used to confirm and substantiate the balances in high risk subrecipients.

In using these techniques, the monitor should exercise discretion and apply the most relevant tests to the given situation.

§ Suggestions for Testing Core Areas §

This section gives examples of how to use the suggested monitoring techniques to test compliance with the required core areas. If the suggested techniques remain the same for high, medium, and low risk subrecipients, then the intensity of the testing should increase and/or the sample size increase as the risk level increases.

Activities Allowed or Unallowed--The primary compliance test to be performed on each program reviewed is whether the activities of the program are allowable under particular program regulations, laws, and provisions of the contract/grant agreement.

The monitor should perform the following tests for low risk subrecipients:

Test to determine through telephone inquires or in writing whether the activities of the program are consistent with the current year grant/contract.

Test to determine whether the program objectives and activities continue to be allowable.

The monitor should perform the following tests for medium risk subrecipients:

Review grants, contracts, and all applicable program guidelines to identify the activities that are allowable.

Test to determine through inquiries and review of documentation whether activities are consistent with the program objectives and are allowable.

The monitor should perform the following tests for high risk subrecipients:

Review grants, contracts, and all applicable program guidelines to identify the activities that are allowable.

Observe, inquire and determine whether activities are consistent with the program objectives and are allowable.

Review contractual relationships that a subrecipient has with any other entity, employee, and/or board member.

Review the documentation which supports the activities under any subcontract and determine if program compliance requirements are being met, if program activities meet program objectives, and if activities are allowable.

Civil Rights--A subrecipient assures that no person on the grounds of handicap or disability, age, race, color, religion, sex, national origin, or any other classification protected at the state and/or federal level be excluded from the participation in, or denied benefits of, or be otherwise subjected to discrimination in the performance of a contract/grant or in the employment practices of the subrecipient.

The monitor should perform the following tests for low risk subrecipients:

Observe whether notices of non-discrimination are posted in conspicuous places, available to all employees and applicants.

Review training provided to subrecipient staff on non-discriminatory issues and policy.

The monitor should perform the following tests for medium and high risk subrecipients:

Observe whether notices of non-discrimination are posted in conspicuous places, available to all employees and applicants.

Review the subrecipients' policies and procedures relevant to all Civil Rights laws, such as, *Title VI, Civil Rights Act of 1964, Title VII, Civil Rights Act of 1964, Section 504, Rehabilitation Act of 1973, Age Discrimination Act of 1975, American Disabilities Act, and Tennessee Public Chapter 502.*

Review Affirmative Action Plan.

Review 504 Self Evaluation and any accommodations made.

Review assurance of compliance signed by the subrecipient.

Confirm with appropriate agencies if any formal complaints against the subrecipient have been filed.

Conduct interviews with program participants regarding the subrecipient's non-discrimination practices.

Review program participants records to determine that eligibility requirements are applied uniformly, applications for assistance are processed equally, outside referrals are made on a non-discriminatory basis, and records are maintained uniformly for all individuals.

Test to determine how the subrecipient disseminates information concerning the program and services to effectively reach minority communities.

Review training provided to subrecipient staff on non-discriminatory issues and policy.

Allowable Costs /Cost Principles--Allowable costs applicable to subrecipients of program funds are described in detail in the cost principles of OMB Circular A-122 and OMB Circular A-87. These circulars describe allowable and unallowable costs and standard methods for calculating indirect cost rates. A state agency may require more stringent guidelines on allowable and unallowable costs. When the requirements of a state agency are more stringent than the federal requirements, then the monitor should apply the requirements of the state agency.

The monitor should perform the following tests for low risk subrecipients:

Conduct desk review. Inspect current contracts and program narratives to determine any changes from prior years' program.

Perform analytical review of pertinent program and financial information including expenditure reports and program progress reports.

Perform analytical review of program and financial information for reasonableness of costs and services rendered.

Perform analytical review of program and financial information reliability and consistency between different quarters and prior years.

Follow up desk review with telephone inquiry to resolve or clarify any questions that arose from desk review.

Request copies of supporting documentation deemed necessary to vouch existence of reported transactions.

Determine if a follow-up onsite review is necessary.

The monitor should perform the following tests for medium and high risk subrecipients:

Test to determine if costs charged to the program are allowable, reasonable and necessary for the performance and administration of the program.

Test to determine if costs are allocable to programs under provisions of applicable state requirements and/or applicable OMB circulars; and that costs allocated to the program are consistent with the benefit received from the program.

Test to determine if costs are applied consistently and conform to generally accepted accounting principles.

Test to determine if costs conform to the limitations of and the exclusions set forth in OMB Circulars A-122 and A-87 or the applicable state guidelines.

Test to determine that costs charged to any program are net of applicable credits, such as discounts, rebates or allowances, recoveries, insurance refunds or adjustments for overpayments.

Vouch to determine if costs are supported by adequate documentation, (such as vendor invoices, canceled checks, time and attendance records, approved purchase orders, receiving reports, and etc.) and represent actual costs, not budgeted or projected amounts.

Eligibility—Each program has specific requirements for eligibility that are unique. These are usually dictated by the laws, regulations, and the provisions of the contract/grant agreements pertaining to the program.

The monitor should perform the following tests for low and medium risk subrecipients:

Test to determine if the program participants were eligible under applicable eligibility guidelines.

Test to determine if program benefit amounts provided to or on behalf of eligible participants were calculated in accordance with program requirements.

The monitor should perform the following tests for high risk subrecipients:

Test to determine if the program participants were eligible under applicable eligibility guidelines.

Test to determine if the program participants continued to be eligible after the initial eligibility

assessment, and if program participants' benefits were discontinued when the period of eligibility expired.

Test to determine if program benefit amounts provided to or on behalf of eligible participants were calculated in accordance with program requirements.

Test to determine if the program participant population and area served were eligible for benefits.

Matching, Level of Effort, Earmarking--Some funding sources have a match requirement, a level of effort requirement and/or an earmarking requirement. Matching requirements refer to contributions specified as an amount or percentage of expenditures that must be borne by the subrecipient. Level of effort refers to a specified level of service to be provided during a defined period; or a specified level of expenditures from other sources for specific activities; or the use of other state and/or federal funds to supplement, but not supplant, non-state and/or non-federal funding of services. Earmarking refers to requirements that define the minimum or maximum amount or percentage of the program's funding that must be used for specified activities provided by the subrecipient.

The monitor should perform the following tests for low risk subrecipients:

Conduct desk review of grant reports

Calculate and determine if required match contributions, level of effort, or earmarking requirements were met.

The monitor should perform the following tests for medium risk subrecipients:

Test to determine if required match contributions, level of effort, or earmarking requirements were met.

Test to determine if matching contributions are from allowable sources.

Test to determine if values placed on in-kind are reasonable and appropriately documented.

Test to determine if state and/or federal funds were used to supplant.

The monitor should perform the following tests high risk subrecipients

Test to determine if required match contributions, level of effort, or earmarking requirements were met.

Test to determine if matching contributions are from allowable sources.

Test to determine if values placed on in-kind are reasonable and appropriately documented.

Test to determine if state and/or federal funds were used to supplant.

Program Income--Program income refers to gross income received by the subrecipient and acquired with program funds. The income is directly generated by the state and/or federally funded programs during the duration of the contract/grant. Examples of program income are fees collected for services, income from the rental of real property, and income from the rental of personal property.

No testing of program income is necessary if subrecipient is deemed to be low risk.

The monitor should perform the following tests for medium and high risk subrecipients:

Test to determine program income was received, identified and recorded properly.

Test to determine program income was used in accordance with all applicable requirements.

Cash Management--Cash management refers to the internal control procedures that minimize the time elapsing between the transfer of funds to subrecipients and the related disbursement. This is applicable to only those grants/contracts that allow advance payments and even payments. It is important to ensure that subrecipients do not have excess funds on hand beyond their immediate needs.

When funds are advanced, state agencies and subrecipients must have procedures to minimize the time elapsing between the transfer of funds to the subrecipient and disbursement. When advance payment procedures are used, the state agency must review and concur with the subrecipient's established procedures.

The monitor should perform the following tests for low risk subrecipients:

Review expenditure reports.

Compare year to date expenditures to cash advances or drawdowns to determine if drawdowns exceed immediate cash needs.

The monitor should perform the following tests for medium and high risk subrecipients:

Test to determine if cash advances or drawdowns are only for amounts necessary for immediate cash needs.

Test to determine if cash does not accumulate beyond the immediate needs of the program.

Davis-Bacon Act--The Davis Bacon Act requires that laborers and mechanics paid under a federal construction contract of \$2,000 or more be paid wages not less than the prevailing wage rates for the locality. This Act will not be applicable to most subrecipients having a grant/contract with the state.

No testing of Davis Bacon Act is necessary for low risk subrecipients.

The monitor should perform the following tests for medium and high risk subrecipients:

Test to determine if the subrecipient has entered into a federal construction contract in the amount of \$2000 or more.

Test to determine if the subrecipient paid the required Department of Labor prevailing rates to laborers and mechanics employed under any federal construction contract.

Equipment and Real Property Management--Equipment refers to tangible non-expendable property having an useful life of more than one year and an acquisition cost of \$1,000 or more per unit. (The limit of the acquisition cost has been increased to \$5,000 or more per unit at the federal level.) Until the state agency revises its requirements regarding acquisition costs, \$1,000 will continue to be the limit. Equipment purchased with federal funds must be used in the program that acquired it or, when appropriate, in other federal programs.

The monitor should perform the following tests for low risk subrecipients:

Conduct desk review of subrecipient's budget to determine whether there was provision of any reported equipment acquisition.

Test to determine whether the program funds used to purchase were within the amount approved for such equipment.

The monitor should perform the following tests for medium and high risk subrecipients:

Test to determine if program funds were used to purchase any equipment.

Test to determine if the subrecipient's policies and procedures for equipment are adequate and consistent with the state and/or federal requirements.

Test to determine if equipment transactions are in compliance with applicable policies and procedures.

Test to determine if equipment records include the following minimal information: description of the equipment, serial number, tag number, source of funding, who holds title to the equipment, acquisition date, acquisition cost, percentage of state and/or federal participation in cost, location, condition, disposal date (if applicable), and sale price (if applicable).

Test to determine if the state agency was reimbursed for the appropriate share of disposed equipment.

Inspect the equipment acquired and determine whether it is consistent with what was planned.

Period of Availability of Funds--This refers to verification that program funds were used only during the period that the funds were authorized to be used.

No testing of period of availability for low risk subrecipients is necessary.

The monitor should perform the following tests for medium and high risk subrecipients:

Inspect grant award and contract to determine the appropriate period of availability of the funds to program

Select a sample of transactions reported to the grant program and vouch whether the underlying obligations occurred during the period of availability.

Select a sample of transactions that were recorded during the period of availability and verify whether underlying obligations occurred during the period of availability.

Select a sample of adjustments to the grant and verify that the adjustments were for transactions that occurred during the period of availability.

Procurement, Suspension and Debarment--This is to verify that subrecipients use the same or more stringent policies and procedures for procurement and to ensure that non-federal entities are prohibited from contracting with or making subawards to parties suspended or disbarred from federal grant program.

No testing of Procurement and Debarment is necessary for low risk subrecipients.

The monitor should perform the following tests for medium and high risk subrecipients:

Test to determine whether procurements were made in compliance with the provisions of A-102 Common Rule and OMB Circular A-110.

Obtain subrecipient's procurement policies and determine whether they are more stringent.

Select and test a sample of procurements to determine compliance with state laws and procedures and other applicable policies.

Verify whether procurements were made through provide full and open competition.

Test a sample of procurements and sub-wards to ascertain if the contracts were entered into with any parties listed on the *List of Parties Excluded From federal Procurement or Nonprocurement Programs*, issued by the General Services Administration.

Real Property Acquisition and Relocation Assistance—This relates to the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970, which provides for uniform and equitable treatment of persons displaced by federally-assisted programs from their homes, businesses or farms.

The monitor should perform the following tests for low risk subrecipients:

Inquire of management whether the subrecipient administers federally assisted programs that involve the acquisition of real property and/or displacement of households or businesses.

The monitor should perform the following tests for medium and high risk subrecipients:

Inquire of management whether the subrecipient administers federally assisted programs that involve the acquisition of real property and/or displacement of households or businesses.

Review records to ascertain whether the right amount of compensation offered based on the appraisal process was

Test records to determine whether the appraisal was reviewed by a review appraiser and that the review appraiser prepared a signed statement which explains the basis of any adjustments.

Test supporting documentation of Residential Relocations to determine whether displaced persons were offered one or more comparable replacement dwellings.

Reporting—This test is to verify that subrecipients use the standard reporting forms as prescribed by OMB or state policy or specific program requirements. These forms may include financial, performance, and special reporting.

The monitor should perform the following tests for high, medium and low risks subrecipients:

Through a desk review, inspect forms used by subrecipient for reporting to determine whether the authorized forms were used.

Specifically review expenditure reports to determine whether they are the authorized forms for Uniform Reporting Requirements Policy 03.

Special Tests and Provisions--In many cases, a program specific supplement, performance standards, or specific program policies will be available to provide specific guidance to the monitor with respect to internal controls, compliance requirements, and suggested procedures. A copy of OMB A-133 Compliance Supplement is in Attachment H. When a program supplement is not available, the monitor should use at a minimum the core tests of the appropriate monitoring level.

DEPARTMENT OF FINANCE AND ADMINISTRATION POLICY 22
Subrecipient Monitoring

Introduction

1. This policy statement 22 establishes a monitoring approach for the State of Tennessee. The policy statement requires the monitoring of subrecipients that receive state and/or federal funds from state departments, agencies, and commissions (hereafter, referred to as state agency).

Applicability

2. This policy statement is applicable to all state agencies that award state and/or federal funds to subrecipients, as defined in paragraph 10, excluding colleges and universities.

Purpose of the Policy

3. The purpose of the policy is to establish a coordinated and centralized monitoring system that defines subrecipient monitoring and the required core monitoring areas; ensures monitoring of all subrecipients; and eliminates duplication of monitoring efforts.

Basis for Authority

4. The Commissioner of the Department of Finance and Administration, in consultation with the Comptroller of the Treasury, is required to establish guidelines for the evaluation by agencies of their systems of internal control as provided by *Tennessee Code Annotated*, Title 9, Chapter 18.

5. In addition, Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*, requires the state to monitor activities of subrecipients and to ensure compliance with program and administrative requirements.

Implementation Guidance

6. The *Tennessee Subrecipient Monitoring Manual* issued by the Department of Finance and Administration, Resource Development and Support Division, provides guidance for monitoring activities in accordance with this policy.

Effective Date

7. The requirements of this policy are effective for the fiscal years beginning after June 30, 1998, and any grants/contracts issued which relate to such fiscal years.

Definition of Monitoring

8. Monitoring is the review process used to determine a subrecipient's compliance with the requirements of a state and/or federal program, applicable laws and regulations, and stated results and outcomes. Monitoring also includes the review of internal control to determine if the financial

management and the accounting system are adequate to account for program funds in accordance with state and/or federal requirements.

Monitoring Staff

9. There should be a separation of duties for all monitoring staff to allow for independence and objectivity.

Definition of Subrecipients

10. A subrecipient is a non-federal entity that expends state and/or federal funds received from the state to carry out a state and/or federal program. There may be unusual circumstances or exceptions to the characteristics of subrecipients and vendors. In making the determination of whether a subrecipient or vendor relationship exists, the substance of the relationship is more important than the form of the agreement. It is not expected that all subrecipient characteristics will be present. Judgment should be used in determining whether an entity is a subrecipient or a vendor. If the contractual relationship with the state meets the vendor criteria, then the state agency must ensure that the procurement, receipt, and payment for goods and services comply with laws, regulations, and the provisions of the contract.

To distinguish a subrecipient from a vendor, use the characteristics below from OMB Circular A-133, Section .210.

Subrecipient Characteristics	Vendor Characteristics
Determines who is eligible to receive state and/or federal financial assistance available through the program administered	Provides the goods and services to many different purchasers
Has its performance measured against whether the objectives of the state and /or federal program are met	Provides goods and services within normal business operations
Has responsibility for programmatic decision making	Operates in a competitive environment
Has responsibility for adherence to applicable state and/or federal program compliance requirements	Provides goods or services that are ancillary to the operation of the state and/or federal program
Uses state and/or federal funds to carry out a program of the state as compared to providing goods or services for a program of the state	Is not subject to compliance requirements of the state and/or federal program

11. Any entity meeting the subrecipient criteria will be subject to monitoring including private non-profit entities, for-profit entities, governmental entities, and state and local governments.

Monitoring Plan - General Rule

12. The plan should identify all subrecipients to be monitored, describe the risk criteria utilized to select and prioritize subrecipients for monitoring purposes, identify full-time equivalents dedicated to monitoring activities, and include a sample monitoring guide for each state and/or federal program. The guide represents minimum monitoring requirements.

13. All state agencies affected by the policy should utilize a risk-based approach for the selection of subrecipients to be monitored, unless specifically prohibited by state and/or federal program guidelines. The risk factors employed in the selection of the subrecipients to be monitored, should be determined by the state agency as deemed appropriate.

14. All state agencies affected by this policy must develop and submit an annual monitoring plan to the Department of Finance and Administration, Division of Resource Development for review, comment and approval by September 30, of each year, starting in 1998.

Core Areas

15. All monitoring activities undertaken by any state agency should include the core monitoring areas: activities allowed or unallowed; civil rights; allowable costs/cost principles; eligibility; matching, level of effort, and earmarking; program income; cash management; Davis-Bacon Act; equipment and real property management; period of availability of funds; procurement, suspension and debarment; real property acquisition and relocation assistance; reporting; and special tests and provisions. The core monitoring areas should be included in the monitoring guides.

Centralization and Coordination

16. The Department of Finance and Administration, Division of Resource Development and Support is the lead agency for the statewide monitoring system. The division will

design, implement, and manage a statewide coordinated monitoring system,

determine monitoring activities and staff to be consolidated and centralized,

provide monitoring services to other state agencies,

review, comment on and approve monitoring plans submitted by state agencies,

provide training and technical assistance on fiscal and program monitoring issues,

develop and maintain a subrecipient management information database.

Requirements for Reporting

17. Each affected state agency shall submit an annual report summarizing its monitoring activities to the Department of Finance and Administration, Division of Resource Development and Support by October 31 of each year, starting in 1999.

18. The Division of Resource Development and Support shall submit an annual report of monitoring activities of all subrecipients to the Commissioner of Finance and Administration and the Comptroller of the Treasury by November 30 of each year, starting in 1999.

Approved:

Commissioner of Finance and Administration

I, John D. Ferguson, hereby approve this Policy Statement 22 of the Department of Finance and Administration, and as such agree with and authorize actions necessary to implement its requirements.

Signed: John D. Ferguson Date: 7/28/98
John D. Ferguson, Commissioner

Approved:

Comptroller of the Treasury

I, William R. Snodgrass, hereby approve this of Policy Statement 22 of the Department of Finance and Administration, and as such agree with and authorize actions necessary to implement its requirements.

Signed: William R. Snodgrass Date: 7/29/98
William R. Snodgrass, Comptroller of the Treasury